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COTY - Q2 2016 Coty Inc Earnings Call

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PRESENTATION

Operator

Good morning, ladies and gentlemen. My name is Kevin and I will be your conference operator today. At this time I would like to welcome everyone to Coty's second-quarter FY16 conference call.

(Operator Instructions)

After the speakers' remarks, there will be a question-and-answer session. As a reminder, this call is being recorded today, Thursday, February 4. Thank you.

I will now turn the call over to Kevin Monaco, Coty's Senior Vice President, Treasurer, Investor Relations. Mr. Monaco, please go ahead.

Kevin Monaco - *Coty Inc. - SVP, Treasurer & IR*

Good morning and thank you for joining us. On today's call, Bart Becht, Chairman and Interim CEO; and Patrice de Talhouet, Executive Vice President and Chief Financial Officer.

Before we begin, I would like to remind you that many of our comments may contain forward-looking statements. Please refer to our press release and our reports filed with the SEC where you will find factors that could cause actual results to differ materially from these forward-looking statements. All discussions of net revenues are in a like-to-like basis. In addition, except where noted, the discussion of our financial results and our expectations do not reflect certain nonrecurring and other charges. You can find the bridge from GAAP to non-GAAP results in the reconciliation tables in the earnings release.

I will now turn the call over to Bart.

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

Thank you, Kevin. This morning we'll provide you with a brief update on the expected merger with the P&G Specialty Beauty Business, other corporate developments, and Q2 and year-to-date results. Then Patrice and I will be pleased to take your questions.

Our efforts right now are all about creating a very healthy platform to Coty to become the strong leader and challenger in the beauty industry that we aim for it to be. This quarter we made good progress on that objective, both on the merger acquisition front and the underlying Coty business side.

Starting with the core Coty business, Q2 showed continued improvement in business fundamentals. Coty revenue trends remain muted with a 1% like-for-like decline and we do expect the Q2 trend to continue for the remainder of the fiscal year as we continue to rationalize non-strategic product lines and businesses. However, and encouragingly, power brands experienced solid mid-single digit growth in the second quarter, very much held by our strategy of focusing and investing in these key brands.

We also continued to show strong momentum in driving profit and cash flow generation. Our year-to-date operating profit grew high single digits with adjusted operating income growing 13% in constant currency, an impressive growth in operating margin. At the same time, our strong networking capital improvement contributed to significant growth in free cash flow generation. These results show that we can continue to build a healthier and better business, despite subdued revenue growth performance.

On the merger and acquisition side, we've made good progress on our Bourjois acquisition. As of today, the local Bourjois businesses have been integrated within Coty local subsidiaries. Also, Bourgeois and Coty processes, as well as information technology, are now fully aligned.

We continue to see good growth opportunities for this brand and remain confident that it will be margin accretive to our call of business in FY17. Since announcing the acquisition of Beamly in the second quarter, these top quality leaders in this digital marketing company have started to engage and work with the Coty brands on several digital campaigns. We are confident by bringing in Beamly's cutting edge digital engagement platform in-house. We will continue to strengthen Coty's marketing and branding efforts.

In addition, we announced on February 1 the completion of the acquisition of the Hypermarcas beauty and personal care business. As a reminder, Hypermarcas is a highly profitable business with operating margins above Coty levels. This transaction will strengthen Coty's exposure to Brazil, which is one of the largest and growing beauty markets in the world.

We believe it will also provide an excellent platform to integrate the existing small Coty business and the sizable P&G Specialty Beauty Business in Brazil. And as announced last week, we signed a new fragrance license agreement with Tiffany & Co, an international renowned jeweler, which we believe will further strengthen our future position as the industry leader on fragrances.

On the P&G Specialty Beauty Business merger, we confirmed the transfer of 10 P&G fragrance licenses, including global power houses such as Hugo Boss, Gucci and Lacoste. We are making excellent progress to close the P&G Specialty Beauty Business merger in the second half of calendar 2016. And we are happy to report that we've received [antitrust] approval from the US, among other countries, and we are actively engaged in discussions with the EU antitrust authorities.

We have also materially advanced on structuring and staffing our future organization and are well advanced in setting up the teams and work streams supporting our IT system requirements and blueprinting the integration plan for the combined businesses. And as I discussed on the last call, we believe the new consumer-centric and category-focused organizational structure, our strong brand portfolio, together with our new leadership team, will position Coty well to realize its ambition of becoming a true leader and challenger in the beauty industry and drive profitable growth and shareholder value over time.

I will now hand over the call to Patrice.

Patrice de Talhouet - *Coty Inc. - EVP & CFO*

Thank you, Bart, and good morning, everyone. Total Q2 net revenues declined 1% like-for-like with an improvement in the fragrant segment trends compared to Q1 and the solid color cosmetic segment growth with [in spite] of the declining US main market. I am happy to report that fiscal year to date the adjusted gross margin increased a very strong 130 basis points to 60.9%, reflecting our continuous effort in driving supply chain efficiencies and reducing discounting activity.

We keep on building a better business, even in the face of soft top line trends, with adjusted operating income growing 5% fiscal year to date, with a much more substantial 13% increase at constant currency. The year-to-date adjusted operating margin and actual rates grew 160 basis points with meaningful margin increase in color cosmetic, up 330 basis points, and skin and body care, up 420 basis points. The fragrance segment margin increased 20 basis points to 20.2%.

As we discussed on the last call, given the market conditions and our global footprint, FX continue to pressure our revenues and operating income. Fiscal year to date, FX lowered net revenues and operating income by over 600 basis points. Our year-to-date adjusted [EPDS] was $0.98 compared to $0.73 in the prior year, reflecting in part the benefit from a favorable tax settlement of $113.3 million this year compared to a $32.5 million settlement in the prior period.

Our global efficiency program remains on track as we have recognized cumulative savings of approximately $170 million for the second quarter of FY16, driven by fixed cost reduction in direct procurement savings, footprint consolidation and more streamlined operations in China. As a reminder, we expect to generate savings of approximately $270 million through FY17.

On the balance sheet, as a reminder, we closed a $4.5 billion credit facilities this quarter to refinance existing Coty debt with new borrowings, subject to longer maturities. As of today, we have swept approximately 40% of our outstanding net floating rate debt into fixed rates. That an all-in cost bid of 3% with an average maturities between three and five years. In addition, certain lenders have committed to loaner to $4.5 billion to an [affiliated] P&G, which is expected to we conveyed to Coty in connection with the expected merger with the P&G Specialty Beauty Business.

With regard to the merger, the initial filing of our registration statement in connection with the transaction is expected to be filed in April. This registration document would include [history] [confidential] information for the beauty brands we are acquiring from P&G through December 31, 2015. Our strong balance sheet and cash flow generation allowed us to continue to advance on our strategic and financial objectives.

I'm very happy to report that fiscal year to date, we generated $517.1 million in operating cash flow and $438.7 million in free cash flow -- each up over $160 million versus the prior year. Supported by these strong cash flow generation, we completed our $700 million share buyback program during the second quarter. In total, this fiscal year we repurchased approximately 26 million Class A shares and we also returned almost $90 million of cash to shareholders as dividends.

We also announced this morning that the board has authorized an incremental $500 million of share repurchase program. We will remain opportunistic in the way we use this authorization. It further supports our commitment to return cash to shareholders.

Finally, on February 1, we completed the acquisition of Hypermarcas Beauty and Personal Care Business, which we believe, as Bart said, we did a great platform to integrate our current and future business in Brazil. We are very excited to expand our footprint in Brazil with this portfolio of leading brands. The execution of the Bourjois acquisition in line with our expectations, as well as the timely closing of the Hypermarcas acquisition, demonstrate our ability to successfully execute on our M&A growth strategy.

Thank you. I will now open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Our first question comes from Bill Schmitz with Deutsche Bank.

Bill Schmitz - *Deutsche Bank - Analyst*

Good morning.

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

Good morning.

Bill Schmitz - *Deutsche Bank - Analyst*

Can you just comment about some of the disclosures and P&G filings? I looked at their last 10-Q and it shows pretty sharp declines in both sales and profits and some of the acquired brands. So I would just love some colors around how much currency impact of that, maybe some of the brands that P&G closed that aren't being transferred that might be in there. Any color would be appreciated.

Patrice de Talhouet - *Coty Inc. - EVP & CFO*

Thanks for the question, Bill. So while we cannot comment on the disclosure of our performance of the business that are not today a part of Coty, we do want to highlight a couple of points. First, it is our understanding that the disclosure in the public filings you reference reflect the sales and profitability of the 47 brands that were apart of the P&G's portfolio and now classified as discontinued operation, rather than the 41 brands that Coty will be acquiring as part of the planned merger. So 4 of the 47 brands have already been sold or discontinued by P&G. Second, we also understand the negative FX impacts accounting for a very substantial component of the reported decline of sales of the 47 brands. Third, we also understand that the organic growth rate of the 41 brands we are acquiring is in line with a like-for-like trends that we are seeing in the Coty business, both for Q2 FY16 and year to date. So I think this gives you a little bit more perspective and color around the disclosure.

Bill Schmitz - *Deutsche Bank - Analyst*

Yes, that's great. And then can you just talk about the Dolce & Gabbana and Christina Aguilera licenses. How big are they? Is there going to be a purchase price adjustment? Does the [collar] get moved? Anything you guys can provide in the public context would also be appreciated.

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

Yes, we are not going to basically disclose that. I think it would be much better is to wait for the S4 filing, which will happen in the second half of April. Because that will really provide the total scope of the business as we will be acquiring with all the financial details. And then shortly after this disclosure, we'll provide an update also in terms of our financial perspective around deal dynamics. But I would say to have a discussion just about Dolce & Gabbana today -- we don't really think is appropriate. I think it would be much better handled when we have all the facts on the table and then have a discussion about what we believe the deal will do for Coty going forward. So that all should happen end April -- latest early May.

Bill Schmitz - *Deutsche Bank - Analyst*

Okay.

Patrice de Talhouet - *Coty Inc. - EVP & CFO*

To build on that on the potential adjustments -- so as per the transaction agreement, you assume debt from P&G Specialty Beauty Business would be adjusted downward to reflect the fact that 10 out of the 12 [valuable] licenses subject to regulatory approval are transferred on all the 12. These downward debt adjustments will be based using a specific and contractually pre-agreed formula that will be disclosed at a later date.

Bill Schmitz - *Deutsche Bank - Analyst*

Okay, great. That's very helpful. And then just a follow-up on the SKU and brand rationalization. Can you just talk about how far along you are on that process and what the impact was, both in the quarter and year-to-date on organic growth, if you have it?

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

Yes. So this will be an ongoing process and it will be reviewed again as part of the P&G merger. Because then clearly we will have an enlarged portfolio and we're going have to, again, reflect in terms of how we deal with the brand portfolio post-merger. So when I say rationalization of the portfolio, I am really referring to several items. First, there is a rationalization of very small brands, which is in the tail of the portfolio. But there's also a discontinuation of certain lines, business lines, product lines of brands. In particular, when they are in places where we don't want to really see them. I'll give you a classic example, selling OPI nail polish in hardware stores is probably not the smartest idea we could do as a Company which is passionate about beauty. And so there is also a rationalization of some businesses in locations where it shouldn't be. So it is both basically a rationalization of small brands and taking out like business situations and to clean that up. And that is an ongoing effort, which will not stop in this quarter or the next quarter and will continue post-merger.

Operator

Thank you. Our next question comes from John Faucher with JPMorgan.

John Faucher - *JPMorgan - Analyst*

Yes, good morning. Thank you. Want to talk about the sequential improvement in the power brands. And then what necessarily do you think is driving that, how sustainable, is it more of a stabilization, or is this something where you could see it getting better and better as we go through? And then a second question on the cash flow, which is the working capital -- appears to be coming a lot from working capital. I think, in particular, payables were better than what we had anticipated and sort of okay. Is that a new level and should we continue to see further improvement in working capital? Thank you.

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

So clearly on power brands, and as you well know, our strategy is very much to continue to focus and invest in these brands behind key innovations. And that's clearly what you're seeing in the second quarter. Having said that, there also is an impact in terms of phasing of launches. As you well know, in the beauty business, but in particular in the fragrance side of the business, which is a substantial chunk of Coty, launch timings around fragrances substantially impact the growth trends. So last year we had a big launch around Calvin Klein in the first quarter, which we didn't have this year. I believe we didn't have the same size of innovation. Having said that, on the other side, Marc Jacobs Decadence very much hits the second quarter. So you are always going to see some fluctuation in the growth rates on the power brands. Having said that, clearly we are very hopeful that we will continue to grow our power brands, in particular, as we rationalize a lot of the businesses outside of the power brands.

Patrice de Talhouet - *Coty Inc. - EVP & CFO*

So on the working capital, John, as you know, I'm coming from a company who is familiar with negative working capital so -- and we are not yet there. So we need to continue on that journey. This being said, it is true that the payables have been the biggest component in the improvement so far. I think there is still some room for improvement in the payables. Now what we really need to tackle is, first, the GSO. There is some room for improvement in a couple of regions. And second, on a more fundamental basis, the inventory level. And this is, as you know, more long-term process, which is really about forecast accuracy, rationalization of the portfolio -- that will definitely help in that regard. So that's more of a long-term. But we are not yet as your working capital becoming within reach of that target, but we are not yet there. And I think there's going to be some further improvement.

John Faucher - *JPMorgan - Analyst*

Great. Thank you.

Operator

Our next question comes from Wendy Nicholson with Citi Research.

Wendy Nicholson - *Citi Investment Research - Analyst*

Hi. I'm sorry if I missed it, but could you walk through what contributed to the gross margin expansion in the quarter? How sustainable that is? Is it cost savings? Is it more favorable mix? That kind of stuff, because it was obviously pretty impressive. Thanks.

Patrice de Talhouet - *Coty Inc. - EVP & CFO*

Sure. So the gross margin improvements is very sustainable in the sense that it's mainly coming from supply chain. And as you know, we have embarked into a productivity program three years ago and we have, on an annual basis, steady improvement from the supply chain. It's coming from procurement savings first. It's also coming from rationalization of the footprint and consolidation of the footprint that we continue to do. So these are very sustainable gross margin improvement. On top of that, there are $2 billion sitting between gross sales and net sales. And we are starting to tackle that with some [early] measurements. This is a long-term process and we are really working on that. And I think there have been some improvement in that regard.

Wendy Nicholson - *Citi Investment Research - Analyst*

And that gap is promotions and that kind of stuff principally?

Patrice de Talhouet - *Coty Inc. - EVP & CFO*

Can you say that again?

Wendy Nicholson - *Citi Investment Research - Analyst*

The gap between the gross sales and the net sales is promotions and discounting and gifts with purchase and that kind of stuff?

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

No, it's -- they are basically historical discounts, which have been agreed with retailers. So it's always a combination of different buckets. And as you well know, even the discount structure depends very much on a country-by-country basis. It's not the same across the globe.

Wendy Nicholson - *Citi Investment Research - Analyst*

Right.

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

So there are promotional discounts in there. There are year-end rebates in there. There are contractual arrangements with retailers in there. So it's a variety, basically, of different components. And even across the countries that would have to discuss with you country-by-country, it's simply the structure differs. If you are interested, we can have a discussion about this at some point in time. But it is a quite involved discussion.

Wendy Nicholson - *Citi Investment Research - Analyst*

And is it fair to say the power brands generally are higher gross margin? Or is there more discounting that goes on with those power brands because they are growing faster and they require more investment?

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

I would say on average the power brands are -- it depends. It's not consistent across the power brand. Some of them definitely are higher margin, but there are also a few which are slightly lower margin than the average. So it's not basically a consistent picture across -- not at this stage.

Wendy Nicholson - *Citi Investment Research - Analyst*

Got it. Okay. Thanks very much. Bye.

Operator

The next question comes from Mark Astrachan with Stifel.

Mark Astrachan - *Stifel Nicolaus - Analyst*

Thanks and good morning, everybody. Wanted to ask a clarifying question of the [Hypermarcas] deal. So when you announced it, I believe it was BRL3.8 billion when it closed earlier this week. It said in the release it was BRL3.5 billion. I guess I'm curious, was there anything to the adjustment there in terms of net piece of working capital, debt adjustments, whatever?

Patrice de Talhouet - *Coty Inc. - EVP & CFO*

So, yes, indeed. You are right. There was some adjustment mechanism based on the working capital and this is the reason why we had the -- this adjustment.

Mark Astrachan - *Stifel Nicolaus - Analyst*

Got it. Okay. And then back on the debt adjustment for the Proctor deal, I appreciate you not wanting to talk about it, but is it fair to assume basically that when we're trying to adjust for [before seeing] the S4, the pre-agreed to multiple that the business would be worth basically would get backed out, whatever that is, per the disclosures as a reflection of anticipated EBITDA? So basically if we're all doing the math, take what we think would be the EBITDA piece, use that multiple, whatever it is, and then just back that number out of the debt. Is that basically it? Or are there any other moving parts to it?

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

No, we're not going to comment on that today. We'll have another session on all the financials end of April, early May. And then a lot of this stuff will be clarified. Even at that point in time, there still will have to be a discussion if we are going to disclose the adjustment formula because that impacts, to some extent, the ability of what happens to this brand on the P&G side. So we would have to get their agreement to disclose this.

So what will be very clear from the S4, which I think is what you'll all be looking for, is what is the scope and what is the structure -- the financial structure of this business? So I think you will all be very happy when you see all of this data. And I think the second part that you're going to get shortly thereafter is our perspective of what the financial impact is of combining the two businesses, which I think also will be what you are looking for. The one thing which I'm not sure we will have at that point in time, and I'm not saying we will not have it, but I just cannot tell you today, is the adjustment formula for the Dolce & Gabbana business not coming to us, because that's something which would have to be agreed to with P&G.

Mark Astrachan - *Stifel Nicolaus - Analyst*

Got it. That's helpful. Then just lastly, more of a holistic sort of longer-term question. Given time to close for the P&G deal, Hypermarcas closing, it seems, fairly quickly, discuss the ability for the business to really hit the ground running on [new co], on Coty plus P&G assets, with a specific view on how quickly you can be back in the market to use the free cash flow to do more deals.

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

Before we start talking about more deals, as you know, we have a few basically to execute at the moment. So I'm going to refrain from commenting on new deals. The Hypermarcas business is really a critical business enabler, both basically in the P&G transaction as well as to establish a long-term interesting business in Brazil. And the reason for that is very, very straightforward. The Coty business is very, very small and therefore has a very sub-critical mass infrastructure. The P&G business is the carve-out and, as a result, has very much of a sub-critical mass infrastructure. Just to give you some perspective, the P&G transaction in Brazil would have come with one sales person. I don't have to tell you that, that's not good enough to run a Brazilian business.

So the Hypermarcas organization is the full-fledged infrastructure business. It has everything. It has a state of the art manufacturing facility and logistics infrastructure. It has also, state of the art basically go-to-market infrastructure and a management team, which has proven to be successful in the market from a market share point of view. So as we speak, we are starting to integrate the Coty business into Hypermarcas. And then once that's done, they will get ready to integrate the P&G business. So Hypermarcas is really the main body that is going to be used in order to integrate and the Coty business and the P&G business. Rather than Hypermarcas not integrated in Coty, really, Coty is being integrated into Hypermarcas. Clearly gets renamed Coty, but just to be crystal clear, from a point of critical mass point of view, that's where the point of gravity lies. And that's very much of an enabler to get the deals done as well as to have a healthy business platform going forward.

Mark Astrachan - *Stifel Nicolaus - Analyst*

Got it. Great. Thank you.

Operator

The next question comes from Lauren Lieberman with Barclays.

Lauren Lieberman - *Barclays Capital - Analyst*

Thanks. Good morning. Just to follow up on the Hypermarcas conversation, Bart, do you have a way of framing it for us? Like how -- to what degree do you think this accelerates your vision of what the business will look like in Brazil? Like is it a three-year accelerator by having the Hypermarcas piece of what Proctor Beauty plus Coty could have been on its own?

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

I would say it is a main accelerator. In markets like Brazil, if you don't have your own manufacturing infrastructure and you own go-to-market infrastructure, it is very difficult to be successful as a major multinational company. In -- because you cannot basically work with third parties in these two areas. So it is a massive accelerator. The fact that Coty doesn't have its own manufacturing infrastructure and has a substandard go-to-market infrastructure, the fact that the P&G business does not really have a local manufacturing infrastructure post deal and doesn't really have good go-to-market infrastructure, is seriously handicapping just taking over the P&G business. So it really is a massive accelerator for us.

The other good thing about Hypermarcas is it's a program management team. They are gaining share as we speak in practically every category that they operate. And so, I genuinely believe that this is a massive accelerator for us to be successful even in -- not in the long-term, even in the medium term in Brazil. Clearly, the first job is to absorb these new businesses -- absorb Coty and the P&G business. That's the first job. Then shortly thereafter, I would hope we're going to see an acceleration in terms of the whole platform.

Lauren Lieberman - *Barclays Capital - Analyst*

Could you also share -- I think some people have questioned just given the movement in the real -- I guess the purchase price and what one pays for emerging market, let alone Brazilian assets currently and current market growth rate. So if you could just share your perspective on the timing and the macro environment, that would be really helpful too.

Patrice de Talhouet - *Coty Inc. - EVP & CFO*

So first, in terms of financing of this acquisition -- so it was financed with the cash on hand and the existing debt facilities that we have. It was financed in dollar but paid in the Brazilian real. And it is clear that we have hedged a vast majority of the price at the time of signature. So I think when -- now -- so that's the first part of the question. On the second part of the question, the way we think about it is really long-term. And so, clearly, this is a great asset. It's significantly eased the merger with the P&G Specialty Beauty Business, as Bart said. It provides the right platform from a go-to-market capabilities, from the manufacturing capabilities. I think we are not ready yet to share the synergies. But in terms of one-off cost and CapEx, it is a significant enabler into the transaction. So we will be able to cost operate with the goods already in Brazil, which is significantly helps.

So I think you need to think about it from a more strategic standpoint and more long-term standpoint. Brazil is one of the key markets. It is the third biggest beauty market in the world. It is the first biggest fragrance market in the world. And the -- it's more long-term view.

Lauren Lieberman - *Barclays Capital - Analyst*

Great. Thanks. And then just one last question on the current Coty business, the drawing down promotional activity a little bit, I thought it was interesting that the fragrance business rate of decline was a little bit less bad than I had expected. And that's notable, particularly, that you were pulling back on promotions during the holiday season. So could you comment on overall market degree of promotional activity, if you felt like there was any kind of following going on in the marketplace, becoming a little bit more rational? Or if it's just, frankly, that your businesses did just fine with a little bit less promotional support than you had expected?

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

Yes. I think -- so first, in terms of growth rate on the fragrance business, clearly there was a differential phasing between the two years in terms of the key launches, like I said before, which had an impact on Q2 relative to Q1. In terms of promotional activity, I would say the overall business is starting to get gradually better at managing gross to net. And by the way, I'm going to retract this number, which Patrice mentioned before, of the $2 billion, because it's not entirely correct. But I would say the key thing is how to manage growth to net. I think, overall, the business is getting better at it and that makes -- I would say in the general market environment, nothing has really changed. We just gotten slightly better at it than we did before. And so you see that reflected in the P&L. So market is not more rational. It is very similar. We just got slightly better at it.

Lauren Lieberman - *Barclays Capital - Analyst*

Okay. Thank you so much.

Operator

Our next question comes from Steph Wissink with Piper Jaffray.

Steph Wissink - *Piper Jaffray & Company - Analyst*

Hi. Good morning, everyone. I'd just like to follow up on Lauren's earlier question, just with respect to the health of the mass channel globally. If you can just talk a little bit about some of the focus that the retailers have been placing on the beauty category, if you expect that to continue here into 2016. And then just secondly, with respect to the Beamly acquisition, just talk a little bit about what we should be looking for in terms of digital engagement or some of the initiatives that you have planned around some of your core brands, what we should be looking for with respect to some of the digital improvements. Thank you.

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

I would say mass basically development is very different by sub-category between fragrance, color, and skin care. So as we all know, in the United States, in particular in fragrance, the most of the growth is in the prestige area and is not in the mass area. And in part is that because of the way mass basically, in particular, behaves in this category. So I think it's more of a channel issue than anything else. So overall there it's not doing a great job. In color cosmetics it's very different. So it very much differs by segment. It's not the same. Mass continues to do well in color cosmetics, does not do very well in fragrance.

Retailers focus on beauty business -- clearly that depends on what retailer you talk about. Some retailers getting increasingly better at it. For instance, the drug trade in the US. Some drug retailers are doing a substantially better business than they did before on the overall beauty business. Digital engagement on core brands -- digital -- we are in a phase where we're trying to transform the business to enter the digital world as accepting it that it is a core component of the entire business. As much as everybody accepts that television, in addition to print and radio, is a normal aspect of doing marketing, we need to have the same on the digital side. And we are on this journey to get the whole organization trained, that digital is just another way of communicating and engaging with our consumers. And this is also where Beamly comes into play. It is there to train and to engage the organization on that journey.

Steph Wissink - *Piper Jaffray & Company - Analyst*

Bart, just a follow-up on that. What is the percentage of spending today in digital and where should we look for that to go over the next couple of years?

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

We don't disclose that and I'm not going to disclose that ever. It is rapidly increasing. That's all I'm going to say.

Steph Wissink - *Piper Jaffray & Company - Analyst*

Okay. Thank you.

Operator

Our next question comes from Dara Mohsenian with Morgan Stanley.

Dara Mohsenian - *Morgan Stanley - Analyst*

Hi. Good morning, guys. Can you give us a sense for A&P spending levels in the quarter? What were they year-over-year? And plans going forward, you've been generating some efficiencies there. So do you think A&P can move down as a percent of sales over time? Or do you think you might need to re-boost spending to drive improving top line trends going forward, both for the heritage Coty portfolio, but also any initial thoughts around the pending P&G brands? Thanks.

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

I'll start and then if Patrice has any further comment. So I think in terms of [A&CP] spending, as you know, we make a distinction between what we really think is strategic spend and non-strategic spend. The difference being that strategic spend is actually what the consumer sees. Non-strategic spend is kind of like the money we waste in the office. So clearly producing a commercial is non-strategic spend because the consumer doesn't see it. So clearly the actual airing of a commercial would be strategic spend. Strategic spend other things would be like if like the furniture that we use in color cosmetics in stores or the beauty assistants that we use on the fragrance business. So those are all basically strategic components.

I can tell you that the strategic spend is substantially increasing, in particular because we've seen -- we've cut the non-strategic spend. And on top of that, even within the strategic spend, we've gotten greater efficiencies in the media buying area. So overall, the output is substantially increasing. Clearly I would have liked to see a bigger response to that in terms of top line growth. Having said that, we are seeing this in some brands. But it is being offset, like I said before, because of a rationalization of the tail and of certain business lines, plus the fact that on certain brands we have not gotten yet to the response that we want to have. Anything you want to add?

Patrice de Talhouet - *Coty Inc. - EVP & CFO*

No. Just on the more long-term perspective, I think the level of investment that in the [overall] A&CP line is roughly in line with what we want to do on the long-term, once again. And because of all the efficiency, because of all the indirect procurement savings and because of the shift of money from non strategic to strategic, as well as the reallocation within the strategic spend to power brands, already this is going to hit significantly in terms of GRIs, the brands that we would like to push to aggregate momentum on the top line. So the level that we currently have is roughly the right level, plus or minus. And but it's more an effort to make sure that we have the right ARI and that we are a bit more diligent in the way we shift the money from non strategic to strategic.

Dara Mohsenian - *Morgan Stanley - Analyst*

Okay. Then on the broader cost savings program in general, the $270 million program, can you give us an update on how much savings have been realized so far? Any thoughts on how the program is progressing and if there could be additional upside over time?

Patrice de Talhouet - *Coty Inc. - EVP & CFO*

So that's a good question. So actually -- so as I said, the sort of savings that we have on the life to date on the program, the committed savings, is $170 million. The target that we have to be achieved at the end of FY17 is $270 million. And we are very confident that we are going to achieve that. Some pieces of the program have been already executed like the China master organization. But other parts are still ongoing. But I'm very confident that we are going to achieve this $270 million target. Once again, as of December 30, 2015, we are at $170 million.

Dara Mohsenian - *Morgan Stanley - Analyst*

Okay. Thanks.

Operator

Our next question comes from Jason Gere with KeyBanc.

Jason Gere - *KeyBanc Capital Markets - Analyst*

Thanks for taking my questions. Actually, both about categories -- specifically in the US. One, I was wondering if you could talk a little bit about the nail category. So while Sally Hanson is doing well -- didn't really mention OPI. I was just wondering, can you talk about what efforts are out there to regrow the nail category? And then the second question, with the -- I guess the good performance of Calvin Klein and Marc Jacobs, can you talk a little bit more between specialty channels and maybe the department stores where I think they were a little bit more promotional over the holidays and how that kind of balanced out for the quarter? Thanks.

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

So in terms of the nail category, clearly there are two very distinctive segments. One is what happens at retail and the other one is what happens in salons. So in terms of retail, which should be the predominant domain of -- or is the domain of Sally Hanson. So the nail category at the moment is largely flat. Sally Hanson, as you well know, has done extremely well behind the launch of Miracle Gel, has gained substantial share. We are going to anniversary that substantial share gain to grow the profile clearly, in terms of color cosmetics for Coty as a result because we are going to index year-on-year. So -- but the nail category is largely flat in the US for the time being while we are gaining share. Clearly, we are working on initiatives to further enhance category growth and market share for Sally Hanson.

OPI is a very different business. OPI really should not be in a very massive way into retail because mostly salon brand. And like I already detailed to you, we are rationalizing some of the OPI's business outside of salon, simply because we believe that this is a salon brand and it's a brand that salon owners should be proud of to use. And we don't want to see a proliferation across many channels of this brand. Here, the effort is very much in terms of driving both category and share within salons. And there are different segments which are relevant in that and we are working on innovations, which it's too early for me to discuss.

Marc Jacobs and Calvin Klein -- so in terms of special or retailers, yes, there is a promotional arena out there in terms of the high end retailers around Christmas, as we well know. In particular because online, I don't have to tell you, is an increasing percentage of the total market. And so that is not changing. As you've seen from our results, we have stayed largely above the fray in this area. And hopefully by investing -- really investing in consumer pool promotion and consumer pool, rather than discounting, we are going to continue to stay above the fray.

Jason Gere - *KeyBanc Capital Markets - Analyst*

Great. Thank you.

Operator

(Operator Instructions)

Our next question comes from Javier Escalante with Consumer Edge Research.

Javier Escalante - *Consumer Edge Research - Analyst*

Hi. Good morning, everyone. I have two questions. One is if you can comment on probably Coty first and then broadly on the industry. How you see Coty performance by channel, because this is the way that you're going to -- I understand you're going to be reporting and reorganizing going forward. So basically professional luxury and consumer. If you can tell us which channels you are doing better and what would be the growth rate vis-a-vis the minus one like-for-like and what is you believe the channel growth in general?

And my second question has to do with -- it was very helpful what you mentioned about Hypermarcas and what is the rationale about Hypermarcas -- the Hypermarcas acquisition. Could you tell us, based on that and also heading toward the integration with Proctor, whether there are some geographies that you feel that you need to invest more ahead of the deal to get that kind of go-to-market capability in place ahead of the deal? Thank you.

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

Yes. So our performance measurement going forward is not going to be so much by channel. It's really going to be by category. So the luxury division is going to be responsible for fragrance and skin care. And so we'll be reporting our fragrance and skin care business. Our consumer beauty business is going to be responsible for color cosmetics, hair coloring and styling as well as body care in the mass retail channel and we're going to report it as much. And finally, we are going to have a professional business, which is going to report. So it is a combination of category and channel.

So in terms of the category performance, I already detailed a little bit what the market growth rates are. So if you look at the overall growth rate of the current business, and I have to exclude hair coloring and retailing styling, because I don't have the data at this stage -- we have some data, but I'm not comfortable enough to discuss those with you today. If you look at the overall market growth rate in beauty in North America and Europe, at the moment it's probably slightly north of 1%. You're going to see a fragrance business, which is flat to marginally up, with basically perceived growing faster than mass. And then you see skin care business, which is now growing at a much more modest rate, in the low single digits, and a color cosmetics business in a category, which is still doing reasonably well, growing several percentage points, with basically nail more flattish and the other parts still showing very healthy growth. And that gives you a rough basically perspective on a category basis.

On basically Hypermarcas and other geographies -- so I don't have to tell you that still today and including the P&G transaction, we are still predominantly in North America and a Western European business, or European business. So which is still the bulk of our business. So we need to, over time, increase our exposure to developing markets. Now I know that this may be most recently not the hottest story in developing markets, but over time, longer term, developing markets in our mind remain markets with higher growth rates. And this is also why, clearly, we did the Hypermarcas transaction because we believe that this is going to be growth accretive over time. And will come at no surprise, considering our minimal presence we still have in Asia and in Africa, Middle East, we also need to expand in those geographies. So I hope that answered your question.

Javier Escalante - *Consumer Edge Research - Analyst*

One follow-up, if I could. Could you comment on travel retail, your own trend, what you are seeing in the overall travel retail channel. That would be helpful.

Bart Becht - *Coty Inc. - Chairman & Interim CEO*

Yes. Travel retail is -- in terms of the overall market, is a much, much more difficult business than it was even a year ago. And a lot of that has to do with traffic, as you can imagine. So it is under more pressure as a market. And clearly we're doing a good job in travel retail, but the overall market conditions are not as favorable as they were. So as you know, this comes and goes with the overall sentiment. So time will tell.

So, I think that was the last question. Can I thank all of you for being on the call? And we are looking forward to having more intense discussion with you in about three months from now when we also have the S4 on the P&G business. Thank you.

Operator

Ladies and gentlemen, this does conclude today's presentation. You may now disconnect and have a wonderful day.